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## Criticism of Rate Cut Mounts

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Federal Reserve Chairman Ben Bernanke faces a perception problem: It looks like he is too ready to respond to a falling stock market.

That criticism was sounded after the Fed moved to cut interest rates Tuesday, in part because of fears that an overseas stock-market plunge would spill over to the U.S. The drumbeat grew more intense yesterday as critics and others confronted the possibility that the global selloff was at least partly a false alarm, reflecting French bank Societe Generale SA's unwinding of a trader's unauthorized bad bets, and due less to economic anxiety.

A Fed official said yesterday that the central bank didn't know of Societe Generale's actions when the Fed cut rates Tuesday morning. But the central bank remains comfortable with its decision, the official added, saying it was based on cumulative evidence of downside risks to the economy, of which mounting volatility in the markets was a symptom. Fed policy makers don't have a view on the appropriate level for stock prices, but are focused on the overall economic outlook, the official said.

But it may be hard for the Fed to persuade the public it didn't overreact to a drop in the stock market.

"It does look like they were snookered into cutting rates," said Lou Crandall, chief economist at research firm Wrightson ICAP LLC. The Fed could argue that responding to the stock drop was appropriate because it threatened financial stability, but that case will be harder to make if the market's drop turns out to be due to a special situation, he said.

After overseas stock markets plunged Monday, which was a holiday in the U.S., Mr. Bernanke convened a meeting of the Fed's policy-setting committee to approve a 0.75-percentage-point cut in the target for the federal-funds rate, at which banks lend to each other. The cut came just a week before the committee was scheduled to meet. The timing prompted some outcries that the Fed panicked.

The Fed has long argued that it only responds to stock prices insofar as they affect the economic outlook. Nonetheless, critics say its hastiness under former Chairman Alan Greenspan to ease when markets quaked amounted to a "Greenspan put," similar to a put option that protects investors against loss. There is now a "Bernanke put," they say.

Fed officials knew they risked feeding that perception. But they decided the risk was outweighed by the need to step up the pace of easing and short-circuit a potential downward spiral in investor

confidence, asset prices and financial stability.

It is unclear how much Societe Generale contributed to Monday's market drop, which began in Asia. Nonetheless, officials say they were motivated not so much by Monday's drop as the cumulative decline in stocks through January; ratings downgrades on bond insurers that could expose banks to further loan defaults; and the self-reinforcing deterioration in home and other asset prices, confidence and economic prospects. Fed officials said yesterday's news doesn't change their view that it is better to err on the side of cutting rates too much because it is harder to undo the damage of cutting too little.

If so, that means the Societe Generale affair shouldn't influence whether the Fed goes ahead and cuts rates at its meeting next week, as expected.

The wisdom of the Fed's rate cuts will likely be judged on the results. If they prove unnecessary, concerns about inflation will return and the Fed will have to boost rates. But if the economy weakens further, its action probably will be viewed as appropriate.

Harvard University economist Martin Feldstein said Mr. Bernanke should have eased around Jan. 10, when the Fed chairman gave a speech highlighting concern about recession, so the move wasn't seen as a response to the stock market. "Given that he didn't do that . . . easing in response to this sharp [stock] decline, not just in the U.S. but globally, was second best but nevertheless a good thing," Mr. Feldstein said.

The perception problem complicates Mr. Bernanke's effort to act, and look, more decisive in addressing the risk of recession.

"You could possibly have nominated him as central banker for the 21st century," given his creative approach to the credit crunch, said James Bianco, president of Bianco Research LLC. "But part of the Fed's job is also political theater as opposed to the actual levers they pull. And he has failed so miserably on the political-theater aspects that it's overwhelming the things he might be doing correctly."